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CIA/RR CB-60-54

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13 December 1960

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CURRENT SUPPORT BRIEF

INVESTMENT LAGS IN EAST GERMANY

OFFICE OF RESEARCH AND REPORTS

CENTRAL INTELLIGENCE AGENCY

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East Germany's prospects in the next few years for economic growth in general, and for the growth of industry in particular, have been weakened considerably as a result of lags in the investment program, increased emigration, and difficulties in agriculture. The production goals of the Seven Year Plan (1959-65), promulgated in late 1959, appeared to be overly ambitious from the start, even in view of plans for investments and employment. Unfavorable developments this year make achievement of these production goals more difficult. The 1960 plan* for investment will not be met, the 1961 investment *61* plan* has been cut, emigration has been larger than anticipated, and the unexpectedly sudden completion of agricultural collectivization is having a negative impact on agricultural production and deliveries.

During the first nine months of 1960, over-all industrial production reportedly increased by 8.4 percent, a respectable rate of growth. A fairly sharp decline in the rate of increase from 12 percent in the first quarter and 10 percent in the first half of the year has occurred, but some decline was undoubtedly planned. The quarterly figures were somewhat lower than scheduled, however, and the annual rate of increase may well be below eight percent, in contrast to a planned rate of slightly over nine percent. The over-all industrial record is of less concern to the East German regime than the fact that the machinery and equipment industries have not achieved their goals. Lags in machinery and equipment production and in construction are directly responsible for failure to meet the investment plan.

The shortage of labor is a major factor in the lags in both investments and production. East German planners did not assume increased emigration during 1960 in drafting their plans for employment; but after declining substantially in 1958-59, emigration has increased this year, partly as a result of the sudden collectivization of agriculture and the continued "socialization" of other private enterprise. By 31 October 1960, the number of emigrants already considerably exceeded the 1959 total of about 145,000, and the net loss of population this year will be at least one percent, most of it of working age. This loss adds significantly to the difficulty of raising employment in priority sectors whenever non-completion of investment projects begins to cause a lag in production. Among the areas most affected by the labor shortage are construction and the investment goods industries.

Lags in Investments

Delays in the production and import of investment goods and the slow pace of construction have kept the investment program behind schedule this year. According to the Central Statistical Administration, investment expenditures at the end of the second and third quarters were running eight and nine percent, respectively, above 1959, compared with the planned increase for the year of 14.5 percent. This lag, added to the 5-percent below-plan level of investments in 1959, suggests that this year's investments will fall perhaps 10 percent below the Seven Year Plan goal.

*The 1960 and 1961 plans mentioned in this paper are those originally drafted as parts of the Seven Year Plan (1959-65).

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Production of machinery and equipment is running below plan, not only on an aggregate basis, but also in some of the most important categories, such as power generators, chemical equipment, and agricultural machinery. The main difficulties seem to be a shortage of labor, an overestimation of productive capacity of existing plants, and, in certain areas, shortages of materials. Plant capacity and labor supply clearly have been more stringent limitations on production than the leadership anticipated in developing the 1960 plans, and attempts to provide stronger workers' incentives, further training and improved management have not compensated for these basic restrictive factors.

The regime hoped, for example, to achieve large increases in labor productivity by forming competitive teams of workers throughout industry and by revising work norms in some branches. However, the workers often are handicapped by outdated equipment and by shortages of materials--a problem which is not new but which continues to limit the growth of production in some industries. Party chief Walter Ulbricht has admitted that the supply of materials has become more "complicated" and that shortages have led to work stoppages. (Inventories of high quality rolled steel at the beginning of 1960 were low, chiefly because the amounts used in the last quarter of 1959 were well above plan--an old story in East Germany.) 48

Another reason for shortages of materials may have been the lag in imports which, during the first three quarters of this year, increased only nine percent, in contrast to a planned annual increase of about 14 percent. Some of these delays have affected supplies of machinery and equipment as well. (For example, the slowdown in the construction of the chemical industry's big project at Schwedt was largely due to the lack of needed imports of chemical equipment.) 148

The construction industry has been even more behind plan this year than last. In the first three quarters of 1960, the reported increase in work of the construction industry was 11 percent, compared with the planned annual increase of over 16 percent. Both the 1960 and the 1961 plans for the number of new housing units to be built have been reduced by about a third, and plans for all construction activity reportedly have been cut for both years. Industrial construction has been particularly slow and probably will not improve significantly in the near future. The East Germans counted heavily on changes in construction methods for increases in productivity, but these changes have not been introduced so rapidly and smoothly as scheduled. The lag in labor productivity behind the Seven Year Plan goals may become even greater during the next year or two. Moreover, there is little chance of securing additional labor to realize planned construction goals.

During the summer the regime apparently concluded that, because of these difficulties, the only hope of reaching the planned level of investments in 1961 was to approach the Soviet government for a large loan. In September an East German mission went to Moscow to request credits of 1.5 billion DME (about \$375 million), with which to finance a foreign trade deficit in 1961. Moscow reportedly refused this request, and the East German regime then felt compelled to reduce planned investments for next year. The first word of a reduction was given to the East German ministries and state secretaries in late September by the State Planning Commission. The cut amounts to 1.4 billion DME (about \$350 million), or about seven percent of planned investments, with construction projects receiving about 70 percent of the cutback. 148

13 December 1960

CIA/RR CB-60-54

Page 3

SECRET

SECRET

(All major sectors of the economy appear to have been affected by the cut in investments. The state investment plan for agriculture and forestry, for example, reportedly was reduced by 200 million DME, or about 24 percent. The chemical industry received a cut of about 160 million DME, or 11 percent, and many of its major projects will be hard hit.) Whereas the shortage of labor is probably the major factor in the cut for low priority construction projects such as those for agriculture, a shortage of equipment is the big reason for the cut in high priority projects such as those in the chemical industry. (Work apparently already has been stopped on the crude oil cracking plant at Schwedt, the synthetic fiber plant at Guben, and the oil cracking plant of the Leuna combine. The expansion of a sulphuric acid plant at Coswig and of polyvinylchloride producing facilities at the Buna works reportedly also was discontinued.)

Effects of the Lag in Investments

One of the short-run effects of the investment lag will be increased difficulties in agriculture. In addition to weakening peasants' incentives, collectivization reduces the amount of family labor available for farming and increases the requirements for agricultural investments, especially in machinery. In most other Bloc countries, collectivization has been supported by increased investments, but in East Germany, agriculture continues to be given a low priority, as indicated by the sharp cut in the 1961 state plan for agricultural investments. (With the completion of collectivization last spring, the regime reportedly modified production and foreign trade plans in an attempt to provide more agricultural machinery, but machinery is still badly lacking, and existing machinery suffers from unsatisfactory servicing and a shortage of spare parts. Insufficient machinery has been a cause of lags in planting and harvesting this year and probably will cause similar problems next year.) As a result of the present disorganized situation in East German agriculture, it may be difficult to prevent a reduction in output and more difficult than before to release any labor for industry in order to offset investment lags.

The long-term effects of the investment lag will probably be seen in the record of over-all economic growth and especially in the growth of industrial production. The rates of growth projected in the Seven Year Plan, adjusted for comparability with Western statistics, amount to about six percent for GNP and eight percent for industry. However, given continued emigration, the lag in investments makes the achievement of such rates of growth very unlikely. The East Germans will face the same difficulties in investments in 1961 as in 1960, and even the reduced investment goal for 1961 is not likely to be achieved. Unless a way can be found to reduce emigration substantially, the labor shortage will become more severe, thereby further increasing the lag in investments behind the schedules of the Seven Year Plan. In turn, cumulative lags in the investment program would severely reduce the growth of fixed assets on which the plans for production in key industries such as chemicals are heavily dependent. Nevertheless, total output in East German industry probably will continue to grow at a respectable rate. Furthermore, although reconsideration of the 1961 plan began before the West German notice of abrogation of the 1961 interzonal trade agreements, the regime has a ready-made scapegoat for any loss of prestige it might suffer as a result of having to lower plan goals.

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The cut in the investment plan probably has not been accompanied by any significant reduction in allocations to consumption, although some cutback of consumption plans eventually may result. At present the regime apparently is determined to proceed with its largely propagandistic plans to "catch up" with West Germany in the per capita consumption of the "most important foodstuffs and consumer goods" by the end of 1961.

13 December 1960

CIA/RR CB-60-54

Page 5

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Sources:

1. Neues Deutschland, 28 Apr 60, 31 Jul 60, 4 Nov 60. U.

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Page 6

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